

BEFORE THE  
POSTAL REGULATORY COMMISSION  
WASHINGTON, DC 20268-0001

DISCOVER NSA

Docket No. MC2011-19

DISCOVER NSA

Docket No. R2011-3

**RESPONSE OF THE UNITED STATES POSTAL SERVICE TO CHAIRMAN'S  
INFORMATION REQUEST NO. 3**  
(March 26, 2013)

Chairman's Information Request (CHIR) No. 3 was issued on March 21, 2013.  
The request sought answers no later than March 26, 2013. Attached are the Postal  
Service's responses to Questions 1 through 10.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

Daniel J. Foucheaux, Jr.

Chief Counsel, Pricing and Product Support

Brandy Osimokun

475 L'Enfant Plaza, S.W.  
Washington, D.C. 20260-1137  
(202) 268-2982, Fax -6187  
Brandy.A.Osimokun@usps.gov  
March 26, 2013

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO CHAIRMAN'S INFORMATION REQUEST NO. 3**

1. The Proposed Amendment provides that “the Postal Service and DFS [Discover Financial Services] agree to amend section II.B.5 as follows” but does not provide any amendatory language (e.g. “amend the agreement by striking section II.B.5 and inserting the following” or “amend section II.B.5 by adding at the end the following”). As a consequence, it is not clear whether the parties intend to replace the existing section II.B.5, add language at the end of the existing section II.B.5, or make some other type of change.
  - a. Please provide the full text of section II.B.5, as the parties intend for it to read after it is amended by the Proposed Amendment.
  - b. If the parties intend to replace the existing section II.B.5 with the language of the Proposed Amendment, please explain how the Revenue Threshold Adjustment will be calculated under the amended agreement. Please provide a full explanation of the calculation, including, at a minimum, the effect of shifts between DFS Eligible First-Class Mail and DFS Eligible Standard Mail and the effect of shifts between DFS Eligible First-Class Mail and Priority Mail.

**RESPONSE:**

- a. It is the parties' mutual intent to add the language in the amendment to the existing section II.B.5. It should read as follows:

Revenue Threshold Adjustment. For every one dollar (\$1) that DFS' total DFS Eligible First-Class Mail postage for the current contract year falls below the total DFS Eligible First-Class Mail postage for the preceding year, the revenue threshold for the current contract year for total DFS Eligible Mail shall be adjusted upward by sixty-five cents (\$0.65). Any rebates received on the preceding year's First-Class Mail postage shall be excluded from the calculation of that year's total DFS Eligible First-Class Mail postage. *In the event, DFS shifts DFS Eligible Mail from First-Class Mail to Priority Mail, the revenue for DFS Eligible First-Class Mail for the current contract year shall be adjusted to include a sum that represents the revenue value of the DFS Priority Mail piece volume, such sum to be calculated by multiplying DFS's priority Mail piece volume by DFS's average DFS Eligible First-Class Mail postage per piece for the current contract year.*

**Only** the DFS pieces that shift to Priority Mail from First-Class Mail are the subject of this amendment. Any other Priority Mail that DFS might send is irrelevant to this agreement. The intended effect of this amendment is to make the third year threshold neutral as to the shift of any and all DFS eligible First Class Mail to Priority Mail.

- b. See response to Question 2a.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO CHAIRMAN'S INFORMATION REQUEST NO. 3**

2. Please confirm that the parties intend to calculate the revenue from DFS Priority Mail that will be included in the revenue for DFS First-Class Mail for a contract year for purposes of the Revenue Threshold Adjustment by multiplying the volume of DFS Priority Mail by the average per-piece postage rate for DFS First-Class Mail for that contract year. If this is not the case, please explain how the revenue from DFS Priority Mail that will be included in the revenue for DFS First-Class Mail for purposes of the Revenue Threshold Adjustment will be calculated under the Proposed Amendment. Please include an example, using hypothetical volumes and postage rates, with the explanation.

**RESPONSE:**

The amendment applies only to the small portion of First-Class Mail volume that DFS will shift to Priority Mail for the limited purpose described in the response to question 3(c) below. The revenue from this Priority Mail volume will not be included in the revenue calculation of the threshold. Rather, in order to make the revenue threshold adjustment neutral for the upgrade of First-Class Mail to Priority Mail, the revenue for DFS' Eligible First-Class Mail will reflect, on a piece by piece basis, the volume of First-Class Mail that shifts to Priority Mail, multiplied by the average First-Class Mail postage per piece for the current year. The product of the calculation representing the shift will be added to the total DFS Eligible First Class Mail to determine whether the revenue threshold adjustment is triggered. If DFS met the threshold for any contract year, the pieces that shifted **would not be included** in the calculation of any rebate DFS' Eligible First-Class Mail.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO CHAIRMAN'S INFORMATION REQUEST NO. 3**

3. The Proposed Amendment asserts that DFS only intends to “upgrade a small portion of its DFS Eligible First-Class Mail to an expedited service.” Notice at 1. However, the Proposed Amendment appears to require that all DFS Priority Mail volume be included in the calculation of revenue for DFS Eligible First-Class Mail.
- a. What portion of DFS Priority Mail volume do the parties intend to include in the calculation of revenue for DFS Eligible First-Class Mail?
  - b. If the parties intend to include all DFS Priority Mail volume in the calculation of revenue for DFS Eligible First-Class Mail, please reconcile that approach with the statement (Notice at 1) that a “small portion” of First-Class Mail volume will shift to Priority Mail.
  - c. If the parties intend to include less than all DFS Priority Mail volume in their calculation of revenue for DFS Eligible First-Class Mail, please explain how the parties intend to determine what that lesser portion will be and why that method is appropriate.

**RESPONSE:**

- a. DFS is going to deliver a new type of credit card to its customers using Priority Mail.

It is **only** the mail that DFS shifts from First-Class Mail to Priority Mail for the delivery of this new credit card that the Postal Service will consider in determining whether the revenue threshold adjustment is triggered. The Postal Service will not consider any other DFS Priority Mail volume or revenue for purposes of this agreement.

- b. See response to Question 3a above.

- c. DFS traditionally mails their credit cards using First-Class Mail, not Priority Mail, so the Postal Service does not anticipate having difficulty tracking the Priority Mail pieces. The Postal Service will require DFS to use a separate permit number to ship these Priority Mail pieces and mail them using the Electronic Verification System (eVS) or the Electronic Documentation System (edoc). This method is appropriate because it allows the Postal Service to isolate the Priority Mail pieces that DFS will

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO CHAIRMAN'S INFORMATION REQUEST NO. 3**

use to mail these credit cards and ensure that it is keeping an accurate accounting of the shifted volume to be credited to the DFS NSA.

Further, the amount that is likely to shift from First Class to Priority Mail is estimated to be roughly less than one percent of total DFS eligible First Class Mail. In this regard, it is noted that DSF does not mail using Priority Mail frequently and is trying to mail these credit cards using an expedited service on an experimental basis.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO CHAIRMAN'S INFORMATION REQUEST NO. 3**

4. No effective date appears to be specified for the Proposed Amendment. Please provide the scheduled effective date for the Proposed Amendment.

**RESPONSE:**

The amendment will be effective the day after the Commission concludes its review of the proposed amendment to the original DFS NSA.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO CHAIRMAN'S INFORMATION REQUEST NO. 3**

5. Please refer to 39 U.S.C. § 3642 and 39 C.F.R. § 3010 subpart D and 3020 subpart B. With reference to these provisions, please explain why it is appropriate to consider volumes of and/or revenues from a competitive product when determining whether an existing market dominant NSA qualifies for a rebate.

**RESPONSE:**

The objective of the original agreement is to maintain the total contribution the Postal Service receives from DFS First-Class Mail and Standard Mail postage, and to provide an incentive for net contribution growth beyond that. The agreement also is intended to promote new growth in Standard Mail that will help offset the expected decline in DFS' First-Class Mail volume.

The NSA penalizes DFS by forcing it to compensate with higher Standard Class volumes for every piece of First Class mail that diverts to electronic delivery. The contract was never intended to penalize DFS, and force it to compensate its decline in First-Class Mail with higher Standard Class volumes for each piece of First Class mail that it diverts to a higher contribution USPS product, regardless whether it is classified as competitive. The amendment to the DFS NSA seeks to remedy the triggering of a penalty for a situation, as described in the response to question 3 above, where DFS upgrades its First-Class Mail to Priority Mail, which that yields more revenue and contribution for the Postal Service than First-Class Mail.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO CHAIRMAN'S INFORMATION REQUEST NO. 3**

6. Please provide proposed language for the MCS to reflect the Proposed Amendment.

**RESPONSE:**

See Attachment A.



**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO CHAIRMAN'S INFORMATION REQUEST NO. 3**

7. Please provide proposed revisions to the existing data collection plan designed to measure the effects of the Proposed Amendment.

**RESPONSE:**

In addition to the current data collection plan, the Postal Service would include the DFS' Priority Mail volume for the just ended contract year, which represents the shift of volumes described in the response to question 3 above. Calculation of the adjustment to the First-Class Mail revenue threshold will be reflected in the existing data collection requirement to explain the adjusted threshold used to establish DFS's eligibility for rebates and payment of penalties, and the calculations underlying the threshold's determination is already required in the current data collection plan.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO CHAIRMAN'S INFORMATION REQUEST NO. 3**

8. Please provide monthly volumes for DFS Priority Mail for the following periods:
  - a. The baseline year (the 12-month period ending on the implementation date).
  - b. Contract year 1.
  - c. Contract year 2 (to the extent practicable).

**RESPONSE:**

Commercially sensitive data. Filed under USPS-MC2011-19/R2011-3/NP1.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO CHAIRMAN'S INFORMATION REQUEST NO. 3**

9. With reference to the baseline, please explain how the DFS Priority Mail volumes will be identified as representing shifts from DFS First-Class Mail to DFS Priority Mail contemplated by the Proposed Amendment.

**RESPONSE:**

DFS will report, and the Postal Service will verify, the volume of First-Class Mail that shifts to Priority Mail for the limited purposed described in the response to question 3 above. The baseline revenue is the total postage from DFS Eligible Mail less any sales rebates earned for the twelve month period preceding February 1, 2011. For the purposes of the agreement, DFS Eligible Mail (mail eligible for discounts) is DFS First-Class Mail and Standard Mail, which includes all First-Class Mail Automation Presort letters and Standard Mail Automation and Enhanced Carrier Route letters that are eligible for the full service Intelligent Mail Barcode discount sent by DFS, by entities in which DFS holds controlling shares, and by their vendors on their behalf.

DFS will not receive a discount on its Priority Mail pieces. The shifted Priority Mail pieces will only be considered for purposes of determining whether the revenue adjustment threshold is triggered.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO CHAIRMAN'S INFORMATION REQUEST NO. 3**

10. The Postal Service states its belief that the Proposed Amendment satisfies 39 U.S.C. § 3622(c)(10). See Notice at 2. Please provide the underlying support for this belief.

**RESPONSE:**

The Postal Service does not believe that the proposed amendment changes the original justification provided to support why this agreement satisfies 39 U.S.C. § 3622(c)(10). The proposed credit of Priority Mail volume to DFS' total First-Class Mail represents less than one percent of DFS' total First-Class Mail pieces, and is only intended to prevent DFS from being penalized for using a higher contribution USPS product.

As previously stated on page 3 of Attachment E to the Notice of the United States Postal Service of Filing of Contract and Supporting Data and Request to Add Discover Financial Services Negotiated Service Agreement to The Market-Dominant Product List, the DFS NSA, including the amendment, addresses the desirability of special classifications. The agreement will generate significant additional contribution to the Postal Service, thus improving its net financial position. In addition, the Postal Service stands ready to negotiate and implement functionally equivalent deals with similarly-situated mailers, and there will be no unreasonable harm to the marketplace from a competitive advantage granted solely to DFS.

**ATTACHMENT C TO REQUEST  
MAIL CLASSIFICATION CHANGES**

**1600<sup>1</sup>        NEGOTIATED SERVICE AGREEMENTS**

[insert the underlined text below]

\*\*\*\*

**1635        DISCOVER FINANCIAL SERVICES, INC. NEGOTIATED  
SERVICE AGREEMENT**

**Eligible Mail:** Eligible First-Class Mail and Standard Mail under this section are defined as all First-Class Mail Automation Presort letters and Standard Mail Automation and Enhanced Carrier Route letters which are eligible for the full-service Intelligent Mail Barcode discount sent by Discover Financial Services, Inc. and by entities in which Discover Financial Services, Inc. holds controlling shares, and by their vendors on their behalf. Eligible mail under this section sent by Discover Financial Services, Inc. will be for the purpose of direct banking and payment services business, including, but not limited to, sales and other promotions run in conjunction with Discover Financial Services' strategic partners or as part of strategic alliances with other entities.

**Eligible Mail Rebates and Calculations:** The following adjusted revenue threshold for otherwise eligible First-Class Mail Automation Presort letters and

---

<sup>1</sup> The sample numbering is included for organizational purposed only. The Commission has not issued a Mail Classification Schedule (MCS) since the original agreement was approved on March 15, 2011 in Order No. 694.

Standard Mail Automation and Enhanced Carrier Route letters must be met before any rebates under this section are payable:

- a. *Baseline Revenue.* The baseline revenue is the total postage from Discover Financial Services, Inc.'s eligible mail less any sales rebates from February 2010 through January 2011.
- b. *Year 1 Revenue Threshold.* Baseline Revenue + 10%.
- c. *Year 2 Revenue Threshold.* Baseline Revenue + 15%.
- d. *Year 3 Revenue Threshold.* Baseline Revenue + 20%.
- e. *Adjusted Revenue Threshold.* For every one dollar that Discover Financial Services, Inc.'s total eligible First-Class Mail postage for the current contract year falls below the total eligible First-Class Mail postage for the preceding year, the revenue threshold for the current contract year for all of Discover Financial Services Inc.'s, total eligible mail will be adjusted upward by sixty-five cents. Any rebates received on the preceding year's First-Class Mail postage shall be excluded from the calculation of that year's total eligible First-Class Mail postage. In the event, DFS shifts DFS Eligible Mail from First-Class Mail to Priority Mail, the revenue for DFS Eligible First-Class Mail for the current contract year shall be adjusted to include a sum that represents the revenue value of the DFS Priority Mail piece volume, such sum to be calculated by multiplying DFS's priority Mail piece volume by DFS's average DFS Eligible First-Class Mail postage per piece for the current contract year.<sup>2</sup>

**Rebate.** Discover Financial Services, Inc. will be eligible for a rebate of 75% of the cumulative postage increase resulting from any price change for its eligible

---

<sup>2</sup> Underlined sentences should be added to the originally proposed MCS language for the Discover Financial Services, Inc. Negotiated Service Agreement.

First-Class Mail letters, and 37.5% of the postage increase resulting from a price change for Standard Mail letters if Discover Financial Services, Inc. meets or exceeds its revenue threshold in that year. The average price increase for Discover Financial Services, Inc.'s eligible First-Class Mail and Standard Mail will be calculated as the change in a Laspeyres index of the relevant price categories for each class, using Discover Financial Services Inc.'s volumes in the preceding contract year as weights.

**Penalties.** Discover Financial Services, Inc. will pay the Postal Service 10% of the difference between the adjusted revenue threshold for the year and their actual postage if Discover Financial Services, Inc. fails to meet the adjusted revenue threshold in the first year of the contract. Penalties for the second and third years of the contract will be agreed between the Postal Service and Discover Financial Services, Inc. 90 days before the end of each previous contract year, to allow room for adjustment based on economic and market conditions.

**Mergers and Acquisitions.** The baseline revenue will be adjusted upward to the extent that Discover Financial Services, Inc. merges with or acquires any entity which mailed either First-Class Mail or Standard Mail or both. The adjustment shall be an amount equal to the total First-Class Mail presort letter and Standard Mail presort letter and Carrier Route letter postage paid by the acquired or merged entity in the twelve months preceding the current contract year.

**Sale or Closure.** The baseline revenue will be adjusted downward to the extent that Discover Financial Services, Inc. sells or closes a division or entity that mailed First Class Mail or Standard Mail or both. The adjustment shall be an amount equal to the total Discover Financial Services, Inc. eligible mail revenue lost from that particular entity or division in the year preceding the sale or closure.

**Termination.** Either the Postal Service or Discover Financial Services, Inc. can terminate this agreement with no penalty within the first nine months of any contract year. At the end of the ninth month, both parties are locked into the contract for the rest of that contract year.

**Expiration.** This agreement expires three years from the implementation date set by the Board of Governors.